EXHIBIT INDEX

2 1 Third Amended Plan of Reorganization of XO Communications, Inc , dated July 22, 2002 (Incorporated herein by reference to exhibit 2 1 filed with the Current Report on Form 8-K/A of XO Communications, Inc , filed on November 26, 2002)

2 2 Plan Supplement, dated October 23, 3003, to the Third Amended Plan of Reorganization of XO Communications, Inc , dated July 22, 2002 (Incorporated herein by reference to exhibit 2 2 filed with the Current Report on Form 8-K/A of XO Communications, Inc , filed on November 26, 2002)

2 3 Order Confirming Third Amended Plan of Reorganization, dated November 15, 2002 (Incorporated herein by reference to exhibit 99 1 filed with the Current Report on Form 8-K/A of XO Communications, Inc , filed on November 26, 2002)

3 1 Amended and Restated Certificate of Incorporation of XO Communications, Inc (Incorporated herein by reference to exhibit 3 1 filed with the Registration Statement on Form 8-A of XO Communications, Inc , filed on February 7, 2003, pursuant to the Securities and Exchange Act)

3 2 Amended and Restated By-laws of XO Communications, Inc (Incorporated herein by reference to exhibit 3 2 filed with the Registration Statement on Form 8-A of XO Communications, Inc , filed on February 7, 2003, pursuant to the Securities and Exchange Act)

4 1 Form of stock certificate of New Common Stock

4 2 1 Series A Warrant Agreement, dated as of January 16, 2003, by and between XO Communications, Inc and American Stock Transfer & Trust Company (Incorporated herein by reference to exhibit 10 1 filed with the Current Report on Form 8-K of XO Communications, Inc , filed on January 30, 2003)

4 2 2 Series B Warrant Agreement, dated as of January 16, 2003, by and between XO Communications, Inc and American Stock Transfer & Trust Company (Incorporated herein by reference to exhibit 10 2 filed with the Current Report on Form 8-K of XO Communications, Inc , filed on January 30, 2003)

4 2 3 Series C Warrant Agreement, dated as of January 16, 2003, by and between XO Communications, Inc and American Stock Transfer & Trust Company (Incorporated herein by reference to exhibit 10 3 filed with the Current Report on Form 8-K of XO Communications, Inc , filed on January 30, 2003)

10 1 1 XO Communications, Inc 2002 Stock Incentive Plan

10 1 2 XO Communications, Inc Retention Bonus and Incentive Plan

10 2 1 Registration Rights Agreement, dated as of January 16, 2003, between XO Communications, Inc and High River Limited Partnership and Meadow Walk Limited Partnership (Incorporated herein by reference to exhibit 10 4 filed with the Current Report on Form 8-K of XO Communications, Inc , filed on January 30, 2003)

10 2 2 Tax Allocation Agreement, dated as of January 16, 2003, between XO Communications, Inc and Starfire Holding Corporation (Incorporated herein by reference to exhibit 10 5 filed with the Current Report on Form 8-K of XO Communications, Inc , filed on January 30, 2003)

10 3 1 Employment Agreement, dated as of January 3, 2000, by and between Nathaniel A Davis and NEXTLINK Communications, Inc (predecessor to XO Communications, Inc) (Incorporated herein by reference to exhibit 10 11 filed with the Annual Report on Form 10-K for the year ended December 31, 1999 of NEXTLINK Communications, Inc and NEXTLINK Capital, Inc)

10 3 2 Letter agreement, dated December 17, 2002, by and among Communications Consultants, Inc , XO Communications, Inc , Eagle River Investments, L L C and R Gerard Salemme

10 3 3 Employment Agreement, dated as of January 13, 2000, by and between Michael S Ruley and XO Communications, Inc (Incorporated herein by reference to exhibit 10 3 3 filed with the Annual Report on Form 10-K for the year ended December 31, 2001 of XO Communications, Inc)

10 4 1 Cost Sharing and IRU Agreement, dated July 18, 1998, between Level 3 Communications, LLC and XO Intercity Holdings No 2, LLC (f/k/a INTERNEXT LLC) (Incorporated herein by reference to exhibit 10 8

filed with the quarterly report on Form 10-Q for the quarterly period ended September 30, 1998 of NEXTLINK Communications, Inc and NEXTLINK Capital, Inc)

10 4 2	Master Agreement, dated August 8, 2002, between Level 3 Communications, Inc and XO Communications, Inc
10 5	Amended and Restated Credit and Guaranty Agreement, dated as of January 16, 2003, among XO Communications, Inc , certain subsidiaries of XO Communications, Inc , the Lenders party thereto from time to time, and Mizuho Corporate Bank, as Administrative Agent
16	Letter from Arthur Andersen LLP to the Securities and Exchange Commission, dated May 15, 2002 (Incorporated herein by reference to exhibit 16 filed with the Current Report on Form 8-K of XO Communications Inc filed on May 16, 2002)
21	Subsidiaries of the Registrant
23 1	Consent of Ernst & Young LLP
23 2	Notice Regarding Lack of Consent of Arthur Andersen
99 1	Certificate pursuant to 18 U S C Section 1350 as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
99 2	Certificate pursuant to 18 U S C Section 1350 as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

REPORT OF ERNST & YOUNG LLP, INDEPENDENT AUDITORS

To the Board of Directors of XO Communications, Inc

We have audited the accompanying consolidated balance sheet of XO Communications, Inc (the "Company") as of December 31, 2002, and the related consolidated statements of operations, stockholders' equity (deficit) and cash flows for the year then ended Our audit also included the financial statement schedule listed in the Index at item 15(a) These financial statements and schedule are the responsibility of the Company's management Our responsibility is to express an opinion on these financial statements and schedule based on our audit The consolidated financial statements and schedule of the Company for each of the two years in the period ended December 31, 2001, were audited by other auditors who have ceased operations, and whose report dated February 6, 2002, expressed an unqualified opinion on those consolidated financial statements and schedules before the restatement adjustments described in Note 5 and included an explanatory paragraph that discussed the substantial doubt about the Company's ability to continue as a going concern

We conducted our audit in accordance with auditing standards generally accepted in the United States Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation We believe that our audit provides a reasonable basis for our opinion

In our opinion, the 2002 financial statements referred to above present fairly, in all material respects, the consolidated financial position of XO Communications, Inc at December 31, 2002, and the consolidated results of its operations and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein

As discussed in Note 5 to the consolidated financial statements, effective January 1, 2002, the Company adopted Statement of Financial Accounting Standards No 142, "Goodwill and Other Intangible Assets"

As discussed in Note 1 to the consolidated financial statements, effective January 16, 2003, the Company was reorganized under a plan of reorganization confirmed by the United States Bankruptcy Court for the Southern District of New York In connection with its reorganization, the Company will apply fresh start accounting in the first quarter of 2003

As discussed above, the financial statements of XO Communications, Inc for the years ended December 31, 2001 and 2000 were audited by other auditors who have ceased operations As described in Note 5, these financial statements have been revised to include the transitional disclosures required by Statement of Financial Accounting Standards No 142, Goodwill and Other Intangible Assets, which was adopted by the Company as of January 1, 2002 Our audit procedures with respect to the disclosures in Note 5 with respect to 2001 and 2000 included (a) agreeing the previously reported net loss to the previously issued financial statements and the adjustments to reported net loss representing amortization expense recognized in those periods related to goodwill and intangible assets that are no longer being amortized to the Company's underlying records obtained from management, and (b) testing the mathematical accuracy of the reconciliation of adjusted net loss to reported net loss, and the related loss-per-share amounts In our opinion, the disclosures for 2001 and 2000 in Note 5 are appropriate However, we were not engaged to audit, review, or apply any procedures to the 2001 or 2000 financial statements of the Company other than with respect to such disclosures and, accordingly, we do not express an opinion or any form of assurance on the 2001 or 2000 financial statements taken as a whole

/s/ Ernst & Young LLP

February 28, 2003

Baltimore, Maryland

The following report is a copy of a report previously issued by Arthur Andersen LLP ("Andersen"), whose report has not been reissued by Andersen. Certain financial information for each of the two years in the period ended December 31, 2001, was not reviewed by Andersen and includes additional disclosures to conform with new accounting pronouncements and SEC rules and regulations issued during such fiscal year, see Item 1, Business, for discussion of risks.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Stockholders of XO Communications, Inc

We have audited the accompanying consolidated balance sheets of XO Communications, Inc ("XO Parent," a Delaware corporation) and subsidiaries (collectively the "Company") as of December 31, 2001 and 2000, and the related consolidated statements of operations, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2001 These financial statements are the responsibility of the Company's management Our responsibility is to express an opinion on these financial statements based on our audits

We conducted our audits in accordance with auditing standards generally accepted in the United States Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation We believe that our audits provide a reasonable basis for our opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of XO Communications, Inc and subsidiaries as of December 31, 2001 and 2000, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2001, in conformity with accounting principles generally accepted in the United States

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern As discussed in Note 1 to the consolidated financial statements, the Company has incurred recurring operating losses and negative cash flows from operating activities, has defaulted on its debt obligations and has begun to implement a proposed recapitalization that contemplates XO Parent filing a voluntary petition for relief under chapter 11 of the United States Bankruptcy Code These matters, among others, raise substantial doubt about the Company's ability to continue as a going concern Management's plans in regard to these matters are also described in Note 1 The accompanying consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or the amounts and classification of liabilities that might otherwise be necessary should the Company be unable to continue as a going concern

Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole The schedule listed in the index of financial statements is presented for purposes of complying with the Securities and Exchange Commission's rules and is not part of the basic financial statements This schedule has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, fairly states, in all material respects, the financial data required to be set forth therein in relation to the basic financial statements taken as a whole

/s/ ARTHUR ANDERSEN LLP

Vienna, VA

February 6, 2002

XO Communications, Inc.
Consolidated Balance Sheets
(Dollars in thousands, except for per share data)

	Pro forma Unaudited Reorganized Company December 31, 2002 (a)	December 31, 2002	December 31, 2001
ASSETS			
Current assets			
Cash and cash equivalents	$ 314,038	$ 314,038	$ 246,189
Marketable securities	246 945	246,945	508,978
Accounts receivable, net of allowance for doubtful accounts of $37,030 and $32,492 respectively	116,541	116,541	216,753
Other current assets	32,654	83,480	101,760
Total current assets	710,178	761,004	1,073,680
Property and equipment net	502,176	2,780,589	3,742,577
Fixed wireless licenses, net	59,508	911,832	947,545
Goodwill, net	—	—	1,876,626
Other intangibles, net	76,171	72,782	153,404
Other assets, net	23,108	59,289	136,633
Total assets	$ 1,371,141	$ 4,585,496	$ 7,930,465
LIABILITIES AND STOCKHOLDERS' (DEFICIT) EQUITY			
Current liabilities not subject to compromise			
Accounts payable	$ 69,729	$ 63,729	$ 156,488
Accrued liabilities	246,048	265,889	341,094
Accrued interest payable	213	213	114,882
Long-term debt in default	—	—	5,109,503
Current liabilities not subject to compromise	315,990	329,831	5,721,967
Current liabilities subject to compromise	—	5,497,207	—
Total current liabilities	315,990	5,827,038	5,721,967
Long-term liabilities not subject to compromise	—	75,242	129,092
Long-term liabilities subject to compromise	—	7,182	—
Long-term debt	500,000	—	—
Other long-term liabilities	80,151	—	—
Total liabilities	896,141	5,909,462	5,851,059
Redeemable preferred stock par value $0 01 per share, 25,000,000 shares authorized 7,856,918 and 7,857,612 shares issued and outstanding on December 31, 2002 and December 31, 2001, respectively, aggregate liquidation preference of $1,693,293 and $1,693,328 on December 31, 2002 and December 31, 2001, respectively			
Subject to compromise	—	1,708,316	—
Not subject to compromise	—	—	1,781,990
Commitments and contingencies			
Stockholders' (deficit) equity			
Common stock, par value $0 02 per share, stated at amounts paid in Class A, 1,000,000,000 shares authorized 331,033,219 and 337,774,204 shares issued and outstanding on December 31, 2002 and December 31, 2001, respectively, Class B, 120,000,000 shares authorized 104,423,158 shares issued and outstanding on both December 31, 2002 and December 31, 2001	475,000	4,628,139	4,628,509
Deferred compensation	—	(8,500)	(37,428)
Accumulated other comprehensive income	—	2,512	10,406
Accumulated deficit	—	(7,654,433)	(4,304,071)
Total stockholders' (deficit) equity	475,000	(3,032,282)	297,416
Total liabilities and stockholders' (deficit) equity	$ 1,371,141	$ 4,585,496	$ 7,930,465

(a) As discussed in footnote 3, the Company emerged from bankruptcy on January 16, 2003 and will be required to adopt the fresh start accounting provisions of SOP 90-7 in the first quarter of 2003 The pro forma balances reflect what the December 31, 2002 balances would have been had the Company applied fresh start accounting as of December 31, 2002

See accompanying notes to consolidated financial statements

XO Communications, Inc.
Consolidated Statements of Operations
(Dollars in thousands, except for share and per share data)

	Year Ended December 31,		
	2002	2001	2000
Revenue	$ 1,259,853	$ 1,258,567	$ 723,826
Costs and expenses			
Cost of service	522,924	527,698	302,666
Selling, operating and general *(excludes stock-based compensation)*	736,925	971,714	730,604
Stock-based compensation	28,928	37,173	48,328
Depreciation and amortization	699,806	1,162,671	617 714
Restructuring and asset write-downs	480,168	509,202	—
In-process research and development	—	—	36,166
Total costs and expenses	2,468,751	3,208,458	1,735,478
Loss from operations	(1,208,898)	(1,949,891)	(1,011 652)
Interest income	16,478	77,938	180,905
Interest expense, net (contractual interest was $501,118 for the year ended December 31, 2002)	(226,451)	(465,401)	(434,122)
Other income (loss), net	(200)	(93,781)	163,570
Reorganization expense, net	(91,121)	—	—
Net loss before extraordinary item and cumulative effect of accounting change	(1,510,192)	(2,431,135)	(1,101,299)
Extraordinary gain on repurchases of debt, net	—	345,010	—
Cumulative effect of accounting change	(1,876,626)	—	—
Net loss	(3,386,818)	(2,086,125)	(1,101,299)
Recognition of preferred stock modification fee, net – reorganization item	78,703	—	—
Gain on repurchases of preferred stock, net	—	376,879	—
Preferred stock dividends and accretion of preferred stock redemption obligation, net (contractual dividend was $98,768 for the year ended December 31, 2002)	(42,247)	(129,671)	(146,356)
Net loss applicable to common shares	$ (3,350,362)	$ (1,838,917)	$ (1,247,655)
Net loss per common share, basic and diluted			
Net loss before extraordinary item and cumulative effect of accounting change	$ (3 42)	$ (6 02)	$ (3 42)
Extraordinary gain on repurchases of debt, net	—	0 86	—
Cumulative effect of accounting change	(4 24)	—	—
Net loss	(7 66)	(5 16)	(3 42)
Recognition of preferred stock modification fee, net – reorganization item	0 18	—	—
Gain on repurchases of preferred stock, net	—	0 93	—
Preferred stock dividends and accretion of preferred stock redemption obligation, net	(0 10)	(0 32)	(0 45)
Net loss per common share, basic and diluted	$ (7 58)	$ (4 55)	$ (3 87)
Weighted average shares, basic and diluted	441,964,342	403,882,956	322,089,883

See accompanying notes to consolidated financial statements

XO Communications, Inc.
Consolidated Statements of Stockholders' Equity (Deficit)
(Dollars in thousands)

	Common Stock				Accumulated Other		
	Shares						
	Class A	*Class B*	*Amount*	Deferred Compensation	Comprehensive Income (Loss)	Accumulated Deficit	Total
Balance at December 31, 1999	150,457,264	117,485,100	$ 1,139,232	$ (85,489)	$ 150,634	$ (1,217,499)	$ (13,122)
Issuance of common stock, options and warrants in acquisitions	77,536,299	—	3,002,309	—	—	—	3,002,309
Issuance of compensatory stock options and restricted stock	200,440	—	30,641	(22,704)	—	—	7,937
Compensation attributable to stock options vesting	—	—	—	36,143	—	—	36,143
Issuance of common stock through employee benefit plans	13,150,088	—	126,604	—	—	—	126,604
Conversion of Class B common stock into Class A common stock	12,070,874	(12,070,874)	—	—	—	—	—
Conversion of 6½% redeemable cumulative preferred stock into Class A common stock	8,595,750	—	93,860	—	—	—	93,860
Comprehensive loss							
Net loss	—	—	—	—	—	(1,101,299)	(1,101,299)
Preferred stock dividends and accretion of preferred stock redemption obligation	—	—	—	—	—	(146,356)	(146,356)
Other comprehensive income - net unrealized holding gains and foreign currency translation adjustments	—	—	—	—	38,870	—	38,870
Realized net gains transferred to current period earnings	—	—	—	—	(206,545)	—	(206,545)
Total comprehensive loss	—	—	—	—	—	—	(1,415,330)
Balance at December 31, 2000	262,010,715	105,414,226	$ 4,392,646	$ (72,050)	$ (17,041)	$ (2,465,154)	$1,838,401
Issuance of common and restricted stock in acquisitions	11,211,416	—	29,055	—	—	—	29,055
Issuance of compensatory stock options	—	—	2,551	(2,551)	—	—	—
Compensation attributable to stock options and restricted stock vesting	—	—	—	37,173	—	—	37,173
Issuance of common stock through employee benefit plans	11,939,685	—	30,899	—	—	—	30,899
Conversion of Class B common stock into Class A common stock	991,068	(991,068)	—	—	—	—	—
Conversion of 6½% redeemable cumulative preferred stock into Class A common stock	1,621,320	—	17,700	—	—	—	17,700
Issuance of common stock related to equity investment, net of offering costs	50,000,000	—	155,658	—	—	—	155,658
Comprehensive loss							
Net loss	—	—	—	—	—	(2,086,125)	(2,086,125)
Gain on repurchases of preferred stock, net	—	—	—	—	—	376,879	376,879
Preferred stock dividends and accretion of preferred stock redemption obligation, net	—	—	—	—	—	(129,671)	(129,671)
Other comprehensive income – net unrealized holding gains and foreign currency translation adjustments	—	—	—	—	22,556	—	22,556
Realized net losses transferred to current period earnings	—	—	—	—	4,891	—	4,891
Total comprehensive loss	—	—	—	—	—	—	(1,811,470)
Balance at December 31, 2001	337,774,204	104,423,158	$ 4,628,509	$ (37,428)	$ 10,406	$ (4,304,071)	$ 297,416

See accompanying notes to consolidated financial statements

XO Communications, Inc.
Consolidated Statements of Stockholders' Equity (Deficit)
(Dollars in thousands)

	Common Stock				Accumulated Other		
	Shares						
	Class A	Class B	Amount	Deferred Compensation	Comprehensive Income (Loss)	Accumulated Deficit	Total
Balance at December 31, 2001	337,774,204	104,423,158	$ 4,628,509	$ (37,428)	$ 10,406	$ (4,304,071)	$ 297,416
Compensation attributable to stock options and restricted stock vesting	—	—	—	28,928	—	—	28,928
Issuance of common stock through employee benefit plans	85,854	—	24	—	—	—	24
Conversion of 6½% redeemable cumulative preferred stock into Class A common stock	3,173	—	35	—	—	—	35
Conversion of Preferred Stock	23,570	—	—	—	—	—	—
Refund of Employee Stock Purchase Plan funds withheld after cancellation (a)		—	(429)	—	—	—	(429)
Cancellation of Craig McCaw's Class A common stock	(6,853,582)	—	—	—	—	—	—
Comprehensive loss							
Net loss	—	—	—	—	—	(3,386,818)	(3,386,818)
Recognition of preferred stock modification fee, net—reorganization item	—	—	—	—	—	78,703	78,703
Preferred stock dividends and accretion of preferred stock redemption obligation, net	—	—	—	—	—	(42,247)	(42,247)
Realized net losses and foreign currency translation adjustments transferred to current period earnings	—	—	—	—	(7,894)	—	(7,894)
Total comprehensive loss	—	—	—	—	—	—	(3,358,256)
Balance at December 31, 2002	331,033,219	104,423,158	$ 4,628,139	$ (8,500)	$ 2,512	$ (7,654,433)	$ (3,032,282)

(a) In the latter half of 2001, the Company's Employee Stock Purchase Plan was cancelled; however employee salary deferrals continued in December 2001, and were subsequently refunded in early 2002

See accompanying notes to consolidated financial statements

XO *Communications*, Inc.
Consolidated Statements of Cash Flows
(Dollars in thousands)

	Year Ended December 31,		
	2002	2001	2000
OPERATING ACTIVITIES:			
Net loss	$ (3,386,818)	$ (2,086,125)	$ (1,101,299)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities			
Depreciation and amortization	699,806	1,162,671	617,714
Stock-based compensation	28,928	37,173	48,328
Non-cash restructuring charges and asset write-downs	477,250	502,737	—
Non-cash reorganization expense, net	89,448	—	—
In-process research and development	—	—	36 166
Net losses (gains) on impairment or sale of investments	—	95,804	(162,429)
Extraordinary gain on repurchases of debt, net	—	(345,010)	—
Cumulative effect of accounting change	1,876,626	—	—
Changes in assets and liabilities net of effects from acquisitions			
Accounts receivable	85,514	(43,254)	(68,761)
Other assets	(21,572)	(66,566)	(42,167)
Other liabilities subject to compromise	195,904	—	—
Other liabilities not subject to compromise	(27,484)	181,693	113,034
Net cash provided by (used in) operating activities	17,602	(560,877)	(559,414)
INVESTING ACTIVITIES:			
Purchases of property and equipment, net	(208,713)	(1,433,746)	(1,380,629)
Prepayment for network assets	—	(120,800)	—
Payments to acquire fixed wireless licenses	—	(206)	(49,502)
Net releases of pledged securities	3,161	150	33,386
Sales of marketable securities and investments	364,069	2,912,454	19,337,905
Purchases of marketable securities	(103,935)	(2,031,072)	(19,381,106)
Cash received for (paid for) divestitures (acquisitions)	3,000	(25,203)	46,940
Investments in unconsolidated entities	—	(10,175)	(71,489)
Net cash provided by (used in) investing activities	57,582	(708,598)	(1,464,495)
FINANCING ACTIVITIES:			
Net proceeds from issuance of redeemable preferred stock	—	—	1,248,901
Borrowings under senior secured credit facility	—	625,000	375,000
Proceeds from issuance of unsecured notes	—	517,500	—
Net proceeds from sale of common stock and modification of preferred stock agreement	—	248,657	—
Proceeds from issuance of common stock under employee benefit plans	—	30,899	98,655
Repurchases of senior notes	—	(201,883)	—
Repurchases of redeemable preferred stock	—	(88,424)	—
Repayments of capital lease and other obligations	(6,079)	(44,124)	(6,809)
Dividends paid on convertible preferred stock	—	(53,778)	(49 984)
Costs incurred in connection with financing activities	—	(14,200)	(17,100)
Net cash (used in) provided by financing activities	(6,079)	1,019,647	1,648,663
Effect of exchange rate changes on cash	(1,256)	3,013	(213)
Net increase (decrease) in cash and cash equivalents	67,849	(246,815)	(375,459)
Cash and cash equivalents, beginning of year	246,189	493,004	868,463
Cash and cash equivalents, end of year	$ 314,038	$ 246,189	$ 493,004

See accompanying notes to consolidated financial statements

XO Communications, Inc.
Notes to Consolidated Financial Statements
December 31, 2002, 2001 and 2000

1. ORGANIZATION AND DESCRIPTION OF BUSINESS

Overview

XO Communications Inc (formerly NEXTLINK Communications, Inc), a Delaware corporation ("XO Parent"), through its subsidiaries, owns and operates an integrated metropolitan and nationwide fiber optic network that provides broadband communication services, local and long distance voice communication services and a wide array of data and integrated data services to business customers in over 60 United States markets Voice services include local and long distance services, calling card and interactive voice response systems Data services include Internet access, private data networking and hosting services XO Parent, through its subsidiaries, also offers combined voice and data services in flat rate "bundled" packages

Organization

The consolidated financial statements include the accounts and activities of XO Parent, and its subsidiaries (collectively referred to as the "Company" or "XO") The consolidated financial statements also include the results of Concentric Network Corporation ("Concentric") commencing June 16, 2000, the date on which Concentric merged with XO The Company, through predecessor entities, was formed in September 1994 As of December 31, 2002, the Company was majority controlled by Craig O McCaw through shares of Class A and Class B common stock held by Eagle River Investments, LLC, an entity controlled by Mr McCaw, and other shares of the Company's Class A and Class B common stock owned or controlled by Mr McCaw

As further discussed in note 2, on June 17, 2002 (the "Petition Date"), XO Parent filed a voluntary petition for relief under Chapter 11 of the United States Bankruptcy Code (the "Bankruptcy Code") with the United States Bankruptcy Court for the Southern District of New York (the "Bankruptcy Court") Accordingly, the accompanying consolidated financial statements have been prepared in accordance with the American Institute of Certified Public Accountants Statement of Position 90-7, "Financial Reporting by Entities in Reorganization under the Bankruptcy Code," ("SOP 90-7") and on a going concern basis which contemplates continuity of operations, realization of assets and liquidation of liabilities in the ordinary course of business In accordance with SOP 90-7, the financial statements for the periods presented distinguish transactions and events that are directly associated with the reorganization from the ongoing operations of the Company The Company conducts its operations through direct and indirect subsidiaries of XO Parent None of these subsidiaries were debtors in the Chapter 11 proceedings

On January 16, 2003 (the "Effective Date"), XO Parent emerged from the Bankruptcy Court proceedings pursuant to the terms of its third amended plan of reorganization (the "Plan of Reorganization") As discussed in note 3, the Company will implement fresh start accounting under the provisions of SOP 90-7 Under the fresh start accounting provisions of SOP 90-7, the fair value of the reorganized Company will be allocated to its assets and liabilities, and its accumulated deficit will be eliminated As discussed in the Pro Forma column on the accompanying balance sheet and in note 3, the implementation of fresh start accounting will result in a substantial reduction in the carrying value of the Company's long-lived assets, including property and equipment, fixed wireless licenses, other intangible assets and other noncurrent assets As a result, the historical financial statements will not be comparable to financial statements of the Company published for periods following the implementation of fresh start accounting

2. REORGANIZATION

The Chapter 11 Petition and Plan of Reorganization

On June 17, 2002, XO Parent filed for protection under Chapter 11 of the Bankruptcy Code in the Bankruptcy Court On November 15, 2002, the Bankruptcy Court confirmed XO Parent's Plan of Reorganization, and, on January 16, 2003, XO Parent consummated the Plan of Reorganization and emerged from its Chapter 11 reorganization proceedings with a significantly restructured balance sheet

During the period immediately preceding and after the filing of XO Parent's Chapter 11 petition, the Company met with a committee of lenders under the $1 0 billion secured credit facility (the "Pre-Petition Credit Facility"), an informal committee of unsecured creditors that represented holders of our senior unsecured notes (and following the filing of the Chapter 11 petition, the official committee of unsecured creditors appointed in the Chapter 11 proceedings) and potential investors to discuss potential restructuring transactions that could be implemented to reorganize XO Parent's capital structure These discussions led to an agreement with the lenders under the Pre-Petition Credit Facility regarding the terms of a Plan of Reorganization that envisioned two potential reorganization structures the first of which was based on, among other things, a proposed cash investment in XO Parent by third parties, which was ultimately abandoned, and the second of which contemplated a stand alone restructuring with no new cash infusion committed in advance The Plan of Reorganization was filed on July 22, 2002 and distributed to creditors of XO Parent eligible to vote in the reorganization

On August 21, 2002, High River Limited Partnership, a limited partnership controlled by Mr Carl Icahn ("High River"), commenced an offer to purchase loans under the company's Pre-Petition Credit Facility at a purchase price of $0 50 for each $1 00 in principal amount thereof Purchases made under this offer, together with the loans under the Pre-Petition Credit Facility that High River previously had acquired, resulted in High River holding approximately 85% of the loans outstanding under the Pre-Petition Credit Facility

The consummation of the Plan of Reorganization resulted in the $1 0 billion of loans under the Pre-Petition Credit Facility being converted into the following

- 90 25 million shares of common stock, par value $0 01 per share, of reorganized XO Parent ("New Common Stock"), and
- $500 million of outstanding principal amount of loans under a restructured secured credit and guaranty agreement (the "New Credit Agreement")

The Plan of Reorganization also resulted in the cancellation of all of XO Parent's pre-bankruptcy senior notes and pre-bankruptcy general unsecured claims in exchange for the following

- 4 75 million shares of New Common Stock,
- warrants to purchase shares up to an additional 23 75 million shares of New Common Stock described below,
- rights to purchase shares of New Common Stock in the rights offering described below; and
- a portion of the cash consideration received by XO Parent in connection with the settlement and termination of the proposed investment transaction that was the basis for the first restructuring alternative contemplated by the Plan of Reorganization (the "Investment Termination Payment")

The warrants consist of

- Series A Warrants to purchase 9 5 million shares of New Common Stock at an exercise price of $6 25 per share,
- Series B Warrants to purchase approximately 7 1 million shares of New Common Stock at an exercise price of $7 50 per share, and
- Series C Warrants to purchase approximately 7 1 million shares of New Common Stock at an exercise price of $10 00 per share

The warrants will expire 7 years after the date of issuance Each series of warrants is identical, except as to the applicable exercise price The exercise price applicable to each respective series of warrants is subject to adjustment in certain events

Under the Plan of Reorganization and after the filing and effectiveness of a registration statement with the Securities and Exchange Commission, XO Parent will issue to certain holders of claims of interests in XO Parent, who hold such claims and/or interests as of the November 15, 2002 record date, rights to subscribe for up to 40,000,000 shares of New Common Stock, at $5 00 per share, for an aggregate purchase price of up to approximately $200 0 million through a rights offering, (the "Rights Offering") In addition, pursuant to the stipulation relating to the settlement of a claim made against XO Parent purportedly on behalf of its stockholders (the "Stockholder Stipulation"), holders of shares of pre-petition class A common stock of XO Parent will receive additional nontransferable rights exercisable for a up to 3,333,333 shares of New Common Stock to the extent that the rights otherwise allocable to such holders in the Rights Offering are exercisable for less than 3,333,333 shares of New Common Stock Accordingly, not less than 40,000,000 and not more than 43,333,333 shares will be offered in the Rights Offering

In addition, under the Plan of Reorganization

- Holders of pre-petition subordinated notes of XO Parent had their securities cancelled, and received a cash payment from High River based upon the amount of the Investment Termination Payment that High River would have been entitled to receive as a holder of the loans under the New Credit Agreement and the right to participate in the Rights Offering; and
- Holders of pre-petition class A common stock of XO Parent had their securities cancelled, and received the right to a portion of the cash consideration pursuant to the Stockholder Stipulation and have the right to participate in the Rights Offering, and
- Holders of pre-petition class B common stock and holders of all series of pre-petition preferred stock of XO Parent had their securities cancelled and received the right to participate in the Rights Offering

Of the 95 0 million shares of New Common Stock distributed on the Effective Date, more than 80% were issued to High River Immediately following this distribution, High River transferred all interest in its New Common Stock to Cardiff Holding LLC, a Delaware limited liability company also controlled by Mr Icahn ("Cardiff") Of the warrants to be distributed under the Plan of Reorganization, XO estimates Cardiff will receive Series A Warrants to purchase approximately 3 0 million shares of New Common Stock, Series B Warrants to purchase approximately 2 3 million shares of New Common Stock, and Series C Warrants to purchase approximately 2 3 million shares of New Common Stock High River assigned its approximately 85% interest in the loans outstanding under the New Credit Agreement to Chelonian Corp ("Chelonian"), which subsequently assigned those loans to Arnos Corp ("Arnos") Both Chelonian and Arnos are controlled by Mr Icahn

Accounting Impact of Chapter 11 Filing

Liabilities subject to compromise reflected in the accompanying consolidated financial statements and the XO Parent stand-alone financial statements represent the liabilities of XO Parent incurred prior to the Petition Date that are with unrelated parties (other than those that are payable to a subsidiary in the XO Parent Stand-Alone Balance Sheet) In accordance with SOP 90-7, liabilities subject to compromise were recorded at the amount allowed on pre-petition claims in the Chapter 11 proceedings Other obligations that are not subject to compromise have retained their historical balance sheet classifications and amounts Liabilities subject to compromise consisted of the following as of December 31, 2002 (dollars in thousands)

Long-term debt	$	5,165,718
Accrued interest and preferred stock dividends		295,820
Pre-petition accounts payable and accrued liabilities		33,640
Capital lease obligations		9,211
Total liabilities subject to compromise		5,504,389
Less long-term liabilities subject to compromise		7,182
Current liabilities subject to compromise	$	5,497,207

At December 31, 2002, there were approximately $34 million of liabilities subject to compromise that had not been settled by the Bankruptcy Court The Company expects to pay approximately $6 million to settle these claims which will result in a reorganization benefit of approximately $28 million

In order to record its debt instruments at the amount allowed by the Bankruptcy Court in accordance with SOP 90-7, as of the Petition Date, XO Parent wrote off all of its debt issuance costs and discounts related to debt (collectively the "Deferred Financing Fees") as a component of reorganization expense Reorganization expense also includes professional fees incurred in connection with the Chapter 11 proceedings, as well as gains or penalties from the settlement or rejection of liabilities subject to compromise and the net gains from the Investment Termination Payment Reorganization expenses for the year ended December 31, 2002 consisted of the following (dollars in thousands)

		Year Ended December 31, 2002
Net loss from the settlement or rejection of liabilities subject to compromise	$	14,916
Net gain from Investment Termination Payment		(16,667)
Deferred Financing Fees		56,270
Professional fees		36,602
Total reorganization expense, net	$	91,121

Under SOP 90-7, XO Parent was required to accrue interest expense during the Chapter 11 proceedings only to the extent that such interest was expected to be paid pursuant to the proceedings Under the Plan of Reorganization, there were no cash payments of interest on the loans outstanding under the Pre-Petition Credit Facility or XO Parent's unsecured notes Therefore, XO Parent ceased accruing interest on the Pre-Petition Credit Facility and on its unsecured notes as of the Petition Date The contractual interest amounts parenthetically disclosed on the accompanying consolidated statement of operations represent the additional interest expense that would have been accrued under the relevant financing agreements had the Company not ceased accruing interest as described above

In accordance with SOP 90-7, XO Parent recorded its preferred stock at the amount allowed by the Bankruptcy Court Accordingly, as of the Petition Date, XO Parent recognized a gain equal to the remaining $81 5 million unamortized balance of a deferred modification fee and wrote off all issuance costs and discounts related to its preferred stock, which resulted in a charge of $2 8 million In addition, the Company stopped accruing preferred stock dividends subsequent to the Petition Date The dividend amounts parenthetically disclosed on the accompanying consolidated statement of operations represent the additional dividends that would have been accrued under the terms of the relevant preferred stock had the Company not ceased accruing such dividends as described above

XO Parent Stand-Alone Financial Statements

In accordance with SOP 90-7, stand-alone financial statements of XO Parent are presented below Such financial statements have been prepared using standards consistent with the Company's consolidated financial statements without eliminating intercompany transactions and without consolidating controlled subsidiaries (dollars in thousands)

XO Communications, Inc.
(XO Parent)
Debtor in Possession
Stand-Alone Balance Sheet
As of December 31, 2002
(Unaudited)

ASSETS	
Current assets	
Pledged securities	$ 1,100
Other current assets	66,764
Total current assets	67,864
Property and equipment, net	65,654
Fixed wireless licenses, net	67,039
Other intangibles, net	79,711
Investment in and notes receivable from subsidiaries, net	8,542,749
Other assets, net	43,638
Total assets	$ 8,866,655
LIABILITIES AND STOCKHOLDERS' EQUITY	
Current liabilities not subject to compromise	$ 50,422
Debt and accrued interest payable to subsidiary subject to compromise	620,389
Current liabilities subject to compromise	5,497,207
Total current liabilities	6,168,018
Long-term liabilities not subject to compromise	62,633
Long-term liabilities subject to compromise	7,182
Total liabilities	6,237,833
Redeemable preferred stock held by and payable to a subsidiary subject to compromise	514,640
Redeemable preferred stock subject to compromise	1,708,316
Stockholders' equity	
Common stock	4,628,139
Deferred compensation	(8,149)
Accumulated deficit	(4,214,124)
Total stockholders' equity	405,866
Total liabilities and stockholders' equity	$ 8,866,655

XO Communications, Inc.
(XO Parent)
Debtor in Possession
Stand-Alone Statement of Operations
(Unaudited)

	Period from the Petition Date of June 17, 2002 through December 31, 2002
Revenue	$ —
Costs and expenses	
Selling operating, and general (excludes stock based compensation)	75,000
Stock-based compensation	12,352
Depreciation and amortization	47,584
Total costs and expenses	134,936
Loss from operations	(134,936)
Reorganization expense, net	(91,121)
Interest income on notes receivable from subsidiaries	286,202
Interest expense	(3,468)
Net income	56,677
Recognition of preferred stock modification fee, net - reorganization item	78,703
Net income applicable to common shares	$ 135,380

XO Communications, Inc.
(XO Parent)
Debtor in Possession
Stand-Alone Statement of Cash Flows
(Unaudited)

		Period From the Petition Date of June 17, 2002 through December 31, 2002
OPERATING ACTIVITIES:		
Net income	$	56,677
Adjustments for non-cash items		
Depreciation and amortization		47,584
Reorganization expense		91,121
Stock-based compensation		12,352
Interest income on notes receivable from subsidiaries		(286,202)
Interest expense		3,468
Changes in assets and liabilities		
Notes receivable from subsidiaries, net		75,000
Net cash used in operating activities		—
Net increase (decrease) in cash and cash equivalents		—
Cash and cash equivalents, beginning of the period		—
Cash and cash equivalents, end of period	$	—

3. FRESH START ACCOUNTING

The Company will adopt the fresh start accounting provisions ("fresh start") of SOP 90-7 during the first quarter of 2003 Under SOP 90-7, the implementation of fresh start reporting is triggered in part by the emergence of XO Parent from its Chapter 11 proceedings Although the effective date of the Plan of Reorganization was January 16, 2003, the Company plans to account for the consummation of the Plan of Reorganization as if it had occurred on January 1, 2003 and implement fresh start reporting as of that date Fresh start requires that the Company adjust the historical cost of its assets and liabilities to their fair value The fair value of the reorganized Company, or the reorganization value, of approximately $1 4 billion was determined based on the sum of the reorganized Company's $500 0 million of debt outstanding under the New Credit Agreement, $475 0 million of New Common Stock as approved by the Bankruptcy Court, and the $425 0 million of other liabilities that were not eliminated or discharged under the Plan of Reorganization

Fresh start requires that the reorganization value be allocated to the entity's net assets in conformity with procedures specified by Accounting Principles Board Opinion ("APB") No 16, "Business Combinations," ("APB No 16") as superseded by Statement of Financial Accounting Standards ("SFAS") No 141, "Business Combinations," ("SFAS No 141") The Company engaged an independent appraiser to assist in the allocation of the reorganization value to the reorganized Company's assets and liabilities by determining the fair market value of its property and equipment, intangible assets and certain obligations related to its facility leases The fair value adjustments impacted current assets, property and equipment, fixed wireless licenses, intangible assets and accrued liabilities A reconciliation of the adjustments to be recorded in connection with the debt restructuring and the adoption of fresh start accounting is presented below (in thousands)

	Predecessor XO December 31, 2002	Debt Restructuring		Fresh Start Adjustments (d)	Reorganized XO Pro forma December 31, 2002 (Unaudited)
ASSETS					
Current assets					
Cash and cash equivalents	$ 314,038	$ —		$ —	$ 314,038
Marketable securities	246,945	—		—	246,945
Accounts receivable	116,541	—		—	116,541
Other current assets	83,480	—		(50,826)	32,654
Total current assets	761,004	—		(50,826)	710,178
Property and equipment net	2,780,589	—		(2,278,413)	502,176
Fixed wireless licenses, net	911,832	—		(852,324)	59,508
Other intangibles, net	72,782	—		3,389	76,171
Other assets, net	59,289	—		(36,181)	23,108
Total assets	$ 4,585,496	$ —		$ (3,214,355)	$ 1,371,141
LIABILITIES AND STOCKHOLDERS' (DEFICIT) EQUITY					
Current liabilities					
Accounts payable	$ 63,729	$ —		$ 6,000	$ 69,729
Accrued liabilities	265,889	—		(19,841)	246,048
Accrued interest payable	213	—		—	213
Total current liabilities	329,831	—		(13,841)	315,990
Current liabilities subject to compromise	5,497,207	(5,461,433)	(a)	(35,774)	—
Long-term debt	—	500,000	(b)	—	500,000
Other long-term liabilities	75,242	—		4,909	80,151
Long-term liabilities subject to compromise	7,182	—		(7,182)	—
Total liabilities	5,909,462	(4,961,433)		(51,888)	896,141
Predecessor XO Redeemable preferred stock -- subject to compromise	1,708,316	(1,708,316)	(a)	—	—
Stockholders' (deficit) equity					
Predecessor XO Common stock	4,628,139	—		(4,628,139)	—
Reorganized XO Common stock and warrants	—	475,000	(c)	—	475,000
Deferred compensation	(8,500)	—		8,500	—
Accumulated other comprehensive income	2,512	—		(2,512)	—
Accumulated deficit	(7,654,433)	6,194,749		1,459,684	—
Total stockholders' (deficit) equity	(3,032,282)	6,669,749		(3,162,467)	475,000
Total liabilities and stockholders' (deficit) equity	$ 4,585,496	$ —		$ (3,214,355)	$ 1,371,141

(a) To record the discharge of indebtedness, including Pre-Petition Credit Facility ($1,000 0 million), pre-petition senior and convertible subordinated notes ($4,165 7 million), accrued interest ($245 2 million), and accrued dividends ($50 6 million) and the elimination of pre-petition Redeemable Preferred Stock ($1,708 3 million) in accordance with the Plan of Reorganization

(b) To record the outstanding principal under the New Credit Agreement, in accordance with the Plan of Reorganization

(c) To record the issuance of New Common Stock and Warrants

(d) To adjust the carrying value of assets, liabilities and stockholders' equity to fair value, in accordance with fresh start accounting

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Review of Significant Accounting Policies

As discussed in note 3, the Company will adopt fresh start accounting during the first quarter of 2003, creating, in substance, per SOP 90-7 a new reporting entity SOP 90-7 also requires that changes in accounting principles required in the financial statements of the emerging entity within twelve months of fresh start reporting should be adopted at the time fresh start reporting is adopted

Principles of Consolidation

The Company's consolidated financial statements include all of the assets, liabilities and results of operations of subsidiaries in which the Company has a controlling interest All inter-company accounts and transactions among consolidated entities have been eliminated

Preparation of Consolidated Financial Statements

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period Management periodically assesses the accuracy of these estimates and assumptions Actual results could differ from those estimates

Cash and Cash Equivalents

The Company considers all highly liquid investments with maturities of three months or less at the time of purchase to be cash equivalents Cash equivalents consist primarily of money market accounts that are available on demand The carrying amount of these instruments approximates fair value due to their short maturities

Marketable Securities

Substantially all of the Company's marketable securities consist of U S government agency issued and other high-grade and highly-liquid securities with original maturities beyond three months The Company classifies investments in debt and equity securities as available-for-sale and records such investments at fair value The fair values are based on quoted market prices Unrealized gains and losses on available-for-sale marketable securities are reported as a separate component of comprehensive income Realized gains and losses for available-for-sale securities are recognized in interest income

Long-Lived Assets

Long-lived assets, including property and equipment, fixed wireless licenses, and intangible assets with definite useful lives to be held and used, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount should be addressed pursuant to SFAS No 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," ("SFAS No 144") SFAS No 144 supersedes SFAS No 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of," ("SFAS No 121") In accordance with implementation requirements, the Company implemented the provisions of SFAS No 144 on January 1, 2002 The criteria for determining impairment for long-lived assets to be held and used are generally consistent with SFAS No 121 Pursuant to SFAS No 144, impairment is determined by comparing the carrying value of these long-lived assets to management's best estimate of future undiscounted cash flows expected to result from the use of the assets The Company believes that no impairment existed under SFAS No 144 as of December 31, 2002 In the event that there are changes in the planned use of the Company's long-lived assets or its expected future undiscounted cash flows are reduced significantly, the Company's assessment of its ability to recover the carrying value of these assets under SFAS No 144 could change As discussed in note 3, the Company will apply fresh start accounting during the first quarter of 2003, which will result in a significant write-down of the Company's long-lived assets

Property and Equipment

Property and equipment is stated at historical cost net of accumulated depreciation Depreciation is calculated on a straight-line basis over the estimated useful lives of the assets beginning in the month telecommunications networks and acquired bandwidth are substantially complete and available for use and in the month equipment and furniture are acquired The estimated useful lives of property and equipment are determined based on historical usage with consideration given to technological changes and trends in the industry that could impact the network architecture and asset utilization Telecommunications networks and bandwidth include the deployment of fiber optic cable and telecommunications hardware and software for the expressed purpose of delivering telecommunications services Costs of additions and improvements are capitalized, and repairs and maintenance are charged to expense as incurred Direct costs of constructing property and equipment are capitalized including interest costs related to construction As discussed in note 3, the Company will apply fresh start accounting during the first quarter of 2003, which will result in a significant write down of property and equipment

Equipment held under capital leases is stated at the lower of the fair value of the asset or the net present value of the minimum lease payments at the inception of the lease For equipment held under capital leases, depreciation is provided using the straight-line method over the shorter of the estimated useful lives of the assets owned or the related lease term

The estimated useful lives of property and equipment are as follows

Telecommunications networks and acquired bandwidth	5-20 years
Furniture, fixtures, equipment, and other	3-5 years
Leasehold improvements	the shorter of the estimated useful lives or the terms of the leases

These useful lives are determined based on historical usage with consideration given to technological changes and trends in the industry that could impact the network architecture and asset utilization This latter assessment is significant because XO operates within an industry in which new technological changes could render some or all of its network related equipment obsolete requiring application of a shorter useful life or, in a worst case, a write off of the entire value of the asset Accordingly, in making this assessment, the Company considers the views of experts within the Company and outside sources regarding the impact of technological advances and trend in the industry on the value and useful lives of its network assets

Fixed Wireless Licenses

Fixed wireless licenses consist of direct costs to acquire fixed wireless licenses The estimated useful life is 20 years, which represents the original ten year license term with one ten year renewal Amortization commences when commercial service using fixed wireless technology is deployed in the license's geographic area Renewal is conditioned upon the satisfaction of certain utilization requirements established by the Federal Communications Commission ("FCC") The Company's current utilization may not be sufficient to satisfy this FCC condition on certain licenses which could impact the FCC's decision to renew As discussed in note 3, the Company will apply fresh start accounting during the first quarter of 2003 which will result in a significant write down of fixed wireless licenses

Goodwill

Goodwill consisted primarily of goodwill from the Concentric merger Effective January 1, 2002, the Company adopted SFAS No 142, "Goodwill and Other Intangible Assets" ("SFAS No 142"), in which goodwill and intangible assets with indefinite lives are no longer amortized but must be tested for impairment annually or more frequently if an event indicates that the asset might be impaired The Company performed the required transitional impairment tests of goodwill as of January 1, 2002, and determined that the goodwill was totally impaired Accordingly, in the first quarter of 2002 the Company recognized a $1,876 6 million charge as a cumulative effect of accounting change to write off all of its goodwill

Other Intangibles

Other intangibles consist primarily of intangibles from the Concentric merger Such costs are amortized using the straight line method of accounting over a period of up to five years As discussed in note 3, the Company will apply fresh start accounting during the first quarter of 2003 which will result in a net increase to other intangibles

Other Assets

Other assets consist primarily of deferred costs associated with the installation of customer services, investments in both publicly traded and privately held companies and pledged securities The Company defers direct labor costs related to customer installations, which are amortized ratably over the estimated customer service period

The Company has investments in entities in which XO has no significant influence These investments are accounted for under the cost method The Company regularly reviews its investment portfolio to determine if any declines in value are other than temporary During 2000 and 2001, the slowing economy had a negative impact on the equity value of companies in the telecommunications sector In light of these circumstances and based on the Company's review of its investment portfolio in this sector, the Company recorded other than temporary impairment charges in other income (loss) of $89 0 million in 2001 and $57 7 million in 2000 with respect to its public and private equity investments

As of December 31, 2002 and 2001, the Company had pledged $1 4 million and $16 6 million, respectively, in certificates of deposit as collateral for outstanding letters of credit The pledged securities are stated at cost, adjusted for accrued interest The fair value of the pledged securities approximates their carrying value

As disclosed in note 3, the Company will apply fresh start accounting during the first quarter of 2003 which will result in a reduction of other assets

Income Taxes

The Company accounts for income taxes in accordance with the provisions of SFAS No 109, "Accounting for Income Taxes," ("SFAS No 109") which requires that deferred income taxes be determined based on the estimated future tax effects of differences between the financial statement and tax bases of assets and liabilities given the provisions of the enacted tax laws Valuation allowances are used to reduce deferred tax assets to the amount considered likely to be realized

Revenue Recognition

Revenues from telecommunication services are recognized when the services are performed, evidence of an arrangement exists, the fee is fixed and determinable and collectibility is probable Service discounts and incentives related to telecommunication services are recorded as a reduction of revenue when granted or ratably over a contract period Fees billed in connection with customer installations and other upfront charges are deferred and recognized ratably over the estimated customer life Revenue from the sale or lease of unlit network capacity is recognized upon consummation of the transaction and the acquirer's acceptance of the capacity in instances when the Company receives upfront cash payments and is contractually obligated to transfer title to the specified capacity at the end of the contract term If the transaction does not meet these criteria, revenue is recognized ratably over the contract term In 2001, approximately 1 5% of XO's total revenue was attributed to sales of unlit network capacity There were no sales of unlit network capacity during 2002 or 2000

The Company establishes valuation allowances for collection of doubtful accounts and other sales credit adjustments Valuation allowances for sales credits are established through a charge to revenue, while valuation allowances for doubtful accounts are established through a charge to selling, operating and general expense The Company assesses the adequacy of these reserves monthly evaluating general factors, such as the length of time individual receivables are past due, historical collection experience, the economic and competitive environment, and changes in the credit worthiness of its customers As considered necessary, the Company also assesses the ability of specific customers to meet their financial obligations to XO and establishes specific valuation allowances based on the amount XO expects to collect from its customers The Company believes that the established valuation allowances were adequate as of December 31, 2002 and 2001 If circumstances relating to specific customers change or economic conditions worsen such that the Company's past collection experience and assessment of the economic environment are no longer relevant, XO's estimate of the recoverability of its trade receivables could be further reduced

In-Process Research and Development

In conjunction with the Concentric merger, the Company allocated $36 2 million of the purchase price to in-process research and development which represented the estimated fair value of incomplete projects based on risk-adjusted future cash flows At the date of the Concentric merger, the development of these projects had not yet reached technological feasibility and the technology had no alternative future uses Accordingly, the entire $36 2 million of acquired in-process research and development was expensed as of the acquisition date

Net Loss Per Share

Net loss per common share, basic and diluted, is computed by dividing loss applicable to common shares by the weighted average number of common shares outstanding for the period In periods of net loss, the assumed common share equivalents for options, warrants and convertible securities are anti-dilutive Assuming exercise or conversion of outstanding stock options, warrants and convertible securities, calculated under the treasury method, diluted shares would have been 549 8 million for 2002, 512 6 million for 2001 and 398 5 million for 2000

As discussed in note 2, the Company emerged from bankruptcy on January 16, 2003 and has a reorganized equity structure In particular, implementation of the Company's Plan of Reorganization resulted in the cancellation of all of the shares of all classes of the Company's common and preferred stock that were outstanding prior to the Petition Date

Stock-Based Compensation

As allowed by SFAS No 123, "Accounting for Stock-Based Compensation," ("SFAS No 123") the Company has chosen to account for compensation cost associated with its employee stock plans in accordance with the intrinsic value method prescribed by APB No 25, "Accounting for Stock Issued to Employees," ("APB No 25") adopting the disclosure-only provisions of SFAS No 123 See note 16 for additional information regarding the Company's stock compensation arrangements

Had compensation costs been recognized based on the calculated fair value of stock options at the date of grant, the pro forma amounts of the Company's net loss applicable to common shares and net loss per common share for the years ended December 31, 2002, 2001 and 2000 would have been as follows (dollars in thousands, except for per share data)

	Year Ended December 31,		
	2002	2001	2000
Net loss applicable to common shares — pro forma	$ (3,351,824)	$ (1,845,882)	$ (1,435 253)
Net loss per common share — pro forma	$ (7 58)	$ (4 57)	$ (4 46)

Comprehensive Loss

Comprehensive loss includes the Company's net loss applicable to common shares, as well as net unrealized gains and losses on available-for-sale investments and foreign currency translation adjustments relating to the Company's European operations Comprehensive loss excludes net realized gains and losses transferred to current period earnings relating to the sale of available-for-sale investments and other than temporary impairment charges

Concentration of Credit Risk

Financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of trade receivables Although the Company's trade receivables are geographically dispersed and include customers in many different industries, a portion of the Company's revenue is generated from services provided to other telecommunications service providers Several of these companies have recently filed for protection under Chapter 11 of the Bankruptcy Code The Company believes that its established valuation and credit allowances are adequate as of December 31, 2002 to cover these risks

Fair Value of Financial Instruments

SFAS No 107, "Disclosure about Fair Value of Financial Instruments" ("SFAS No 107"), requires disclosure of fair value information about financial instruments, for which it is practicable to estimate the value The carrying amounts for the Company's financial instruments classified as current assets and liabilities approximate their fair value due to their short maturities as a result of the Company's emergence from bankruptcy, the holders of the Company's debt and equity instruments received certain rights and securities as described further in note 2

New Accounting Pronouncements

In June 2001, the Financial Accounting Standards Board ("FASB') issued SFAS No 143, "Accounting for Asset Retirement Obligations," ("SFAS No 143") which requires an entity to recognize the fair value of a liability for an asset retirement obligation in the period in which a legal or contractual removal obligation is incurred if a reasonable estimate of fair value can be made If a reasonable estimate of fair value cannot be made in the period the asset retirement obligation is incurred, SFAS No 143 requires the liability to be recognized when a reasonable estimate of the fair value can be made The provisions of SFAS No 143 are effective for financial statements issued for fiscal years beginning after June 15, 2002 As required by SOP 90-7, the Company will implement SFAS No 143 during the first quarter of 2003 in conjunction with the implementation of fresh start accounting The accompanying pro forma balance sheet and note 3 includes an estimated asset retirement obligation of $21 4 million

In April 2002, the FASB issued SFAS No 145, "Rescission of FASB Statements No 4, 44, and 64, Amendment of FASB Statement No 13, and Technical Corrections as of April 2002", ("SFAS No 145") which eliminates the requirement to report material gains or losses from debt extinguishments as an extraordinary item, net of any applicable income tax effect, in an entity's statement of operations SFAS No 145 instead requires that a gain or loss recognized from a debt extinguishment be classified as an extraordinary item only when the extinguishment meets the criteria of both "unusual in nature" and "infrequent in occurrence" as prescribed under APB Opinion No 30, "Reporting the Results of Operations - Reporting the Effects of Disposal of a Segment of a Business, and

Extraordinary, Unusual and Infrequently Occurring Events and Transactions" ("APB No 30") The provisions of SFAS No 145 are effective for fiscal years beginning after May 15, 2002 with respect to the rescission of SFAS No 4 and for transactions occurring after May 15, 2002, with respect to provisions related to SFAS No 13 The Company has recognized extraordinary gains from debt repurchases in 2001 and has determined that the classification of such gains as extraordinary items will change under SFAS No 145 when XO implements fresh start accounting in accordance with SOP 90-7

In June 2002, the FASB issued SFAS No 146, "Accounting for Costs Associated with Exit or Disposal Activities", ("SFAS No 146") which requires that costs, including severance costs, associated with exit or disposal activities be recorded at their fair value when a liability has been incurred Under previous guidance, certain exit costs, including severance costs, were accrued upon managements' commitment to an exit plan, which is generally before an actual liability has been incurred The Company will apply the provisions of SFAS No 146 to any exit or disposal activities initiated after December 31, 2002

In December 2002, the FASB issued SFAS No 148, "Accounting for Stock-Based Compensation-Transition and Disclosure", ("SFAS No 148") which amends SFAS No 123, to provide alternative methods of transition to SFAS No 123's fair value method of accounting for stock-based employee compensation SFAS No 148 also amends the disclosure provisions of SFAS No 123 and APB Opinion No 28, "Interim Financial Reporting," ("APB No 28")to require disclosure in the summary of significant accounting policies of the effects of an entity's accounting policy with respect to stock-based employee compensation on reported net income and earnings per share in annual and interim financial statements While SFAS No 148 does not amend SFAS No 123 to require companies to account for employee stock options using the fair value method, the disclosure provisions of SFAS No 148 are applicable to all companies with stock-based employee compensation, regardless of whether they account for that compensation using the fair value method of SFAS No 123 or the intrinsic value method of APB No 28 The provisions of SFAS No 148 are effective for fiscal years beginning after December 15, 2002 with respect to the amendments of SFAS No 123 and effective for financial reports containing condensed financial statements for interim periods beginning after December 15, 2002 with respect to the amendments of APB No 28 The Company will implement SFAS No 148 effective January 1, 2003 regarding disclosure requirements for condensed financial statements for interim periods Management is currently evaluating the impact of the fair value method of accounting for stock-based compensation on the Company's results of operations and financial position

5. CUMULATIVE EFFECT OF ACCOUNTING CHANGE

In July 2001, the FASB issued SFAS No 142, which revises the accounting for purchased goodwill and intangible assets and supersedes APB Opinion No 17, "Intangible Assets" ("APB No 17") Under SFAS No 142, goodwill and intangible assets with indefinite lives are no longer amortized but must be tested for impairment annually or more frequently if an event indicates that the asset might be impaired This impairment test under SFAS No 142 is based on fair values determined by using market prices, current prices for similar assets and liabilities, or a discounted cash flow methodology Intangible assets with definite useful lives continue to be amortized over their useful lives

SFAS No 142 required that the initial impairment analysis of goodwill be completed by June 30, 2002 If however, events or changes in circumstances indicate that goodwill of a reporting unit might be impaired before June 30, 2002, goodwill was required to be tested for impairment when this indication of possible impairment arises The Company performed the required transitional impairment tests of goodwill as of January 1, 2002, and determined that the value of its goodwill was totally impaired Accordingly, in the first quarter of 2002, the Company recorded a $1,876 6 million charge as a cumulative effect of accounting change to write-off all of its goodwill The pro forma impact on net loss before cumulative effect of accounting change for the year ended December 31, 2002, 2001, and 2000 compared to the actual results for the same period is as follows (dollars in thousands, except for per share data)

	2002	2001	2000
Net loss before extraordinary item and cumulative effect of accounting change	$ (1,510,192)	$ (2,431,135)	$ (1,101,299)
Goodwill amortization	—	595,601	323,109
Adjusted net loss before extraordinary item and cumulative effect of accounting change	$ (1,510,192)	$ (1,835,534)	$ (778,190)

Net loss per common share before extraordinary item and cumulative effect of accounting change, basic and diluted			
Reported net loss before extraordinary item and cumulative effect of accounting change	$ (3 42)	$ (6 02)	$ (3 42)
Goodwill amortization	—	1 47	1 00
Adjusted net loss per common share before extraordinary item and cumulative effect of accounting change, basic and diluted	$ (3 42)	$ (4 55)	$ (2 42)

6. RESTRUCTURING CHARGES AND ASSET WRITE-DOWNS

On August 8, 2002, the Company entered into a Master Agreement with Level 3 Communications, Inc ("Level 3"), which amends various agreements related to XO's acquisition of fiber networks in the United States from Level 3 and the recurring maintenance thereon (the "Master Agreement") Beginning on January 1, 2003 and continuing over the remaining term of the initial agreement, the Company's operating and maintenance fees as well as fiber relocation charges will be reduced from approximately $17 0 million annually to a fixed rate of $5 0 million annually In exchange for this reduction and certain other concessions, effective as of February 11, 2003, the closing date for the transaction, the Company surrendered its indefeasible right to use an empty conduit and six of the 24 fibers previously acquired from Level 3 Because the Company had committed to this plan of disposal and believed at the time that XO entered into the Master Agreement that consummation of the contemplated transaction was probable, the Company recorded a $477 3 million non-cash write-down of these assets during the third quarter of 2002 Pursuant to applicable accounting principles, the write-down is based on the book value of the surrendered facilities and does not reflect the future benefits to be received by the Company under the Master Agreement

During the second half of 2001, the Company implemented a plan to restructure certain of its business operations The restructuring plan included reducing the Company's discretionary spending, capital expenditures and workforce based on its assessment of current and future market conditions and the divestiture of its European operations As a result of the restructuring plan, the Company recorded $509 2 million of estimated restructuring charges during the year ended December 31, 2001 The Company continued to restructure its operations, reducing its workforce by approximately 350 additional employees, the majority of which were employed in network operations, sales and marketing and information technology, and recorded a $2 9 million restructuring charge related to involuntary termination severance liabilities in the second quarter of 2002 These employees were notified of their termination of employment in the second quarter of 2002 and the employment of the majority of the notified employees was terminated by June 30, 2002 As of December 31, 2002, the remaining restructuring accrual was $79 0 million, which relates primarily to payments due to landlords on exited leased facilities The restructuring accrual has decreased from $125 8 million as of December 31, 2001 primarily due to payments associated with exited leased facilities

7. MARKETABLE SECURITIES

Marketable securities consisted of the following (dollars in thousands)

	December 31, 2002	December 31, 2001
U S Government and agency notes and bonds	$ 246,945	$ 242,048
Corporate notes and bonds	-	266,930
	$ 246,945	$ 508,978

8. PROPERTY AND EQUIPMENT

Property and equipment consisted of the following components (dollars in thousands)·

	December 31, 2002	December 31, 2001
Telecommunications networks and acquired bandwidth	$ 2,920,819	$ 2,832,878
Furniture, fixtures, equipment, and other	656,994	758,022
	3,577,813	3,590,900
Less accumulated depreciation	1,165,216	795,739

	2,412,597	2,795,161
Network construction-in-progress	367,992	947,416
	$ 2,780,589	$ 3,742,577

As discussed in note 3, the Company will apply fresh start accounting during the first quarter of 2003, which will result in a significant write down of property and equipment and the associated depreciation expense in future periods During 2002, 2001 and 2000, depreciation expense was $598 5 million, $447 0 million and $223 8 million, respectively During 2002, 2001 and 2000, the Company capitalized interest on construction costs of $11 1 million, $51 6 million, and $31 0 million, respectively

As of December 31, 2002, the Company owned a North American inter-city network with a carrying value of $260 5 million The inter-city network requires the purchase and installation of optical networking equipment in order for the fiber to be "lit" and operationally ready for its intended use The Company has postponed lighting this network and in the interim has purchased Level 3 wavelength capacity to provide inter-city transport As a result, the inter-city network has not been placed into service, is not being depreciated and is included in network construction-in-progress as of December 31, 2002

9. OTHER INTANGIBLES

Intangible assets with definite useful lives consisted of the following (dollars in thousands)

	December 31, 2002			December 31, 2001		
	Gross Carrying Amount	Accumulated Amortization	Net Book Value	Gross Carrying Amount	Accumulated Amortization	Net Book Value
Acquired technology	$ 130,515	$ (84,336)	$ 46,179	$ 141,541	$ (56,027)	$ 85,514
Customer lists.	123,745	(105,635)	18,110	124,873	(80,845)	44,028
Other	35,413	(26,920)	8,493	48,731	(24,869)	23,862
Total intangible assets	$ 289,673	$ (216,891)	$ 72,782	$ 315,145	$ (161,741)	$ 153,404
Fixed wireless licenses	$ 997,942	$ (86,110)	$ 911,832	$ 997,942	$ (50,397)	$ 947,545

As discussed in note 3, the Company will apply fresh start accounting during the first quarter of 2003, which will result in a significant write down of other intangibles and the associated amortization expense Amortization expense for the years ended December 31, 2002, 2001 and 2000 was $101.3 million, $715 7 million and $393 9 million, respectively Fixed wireless licenses are amortized when commercial service using the wireless technology is deployed in the license's geographic area At December 31, 2002, $635 3 million of the fixed wireless licenses are being amortized

10. ACCRUED LIABILITIES

Accrued liabilities consisted of the following components (dollars in thousands)

	December 31,	
	2002	2001
Accrued compensation	$ 58,551	$ 73,807
Accrued telecommunications costs	52,803	40,955
Accrued construction	1,123	27,552
Other accrued liabilities	153,412	198,780
	$ 265,889	$ 341,094

11. LONG-TERM DEBT

As of December 31, 2002, the carrying value of the Company's long-term debt was $5.2 billion including $3 7 billion in pre-petition senior notes, $0 5 billion in pre-petition convertible subordinated notes, and $1 0 billion outstanding under the Pre-Petition Credit Facility, all of which are classified as current liabilities subject to compromise The Company ceased making all scheduled interest payments due under the terms of its senior unsecured notes effective December 1, 2001, and its subordinated unsecured notes in February 2002 Consequently, as of December 31, 2001, the Company was in default on certain unsecured notes and had triggered cross-default provisions under the Pre-Petition Credit Facility and the indentures under which all other senior notes were issued, so the entire $5 2 billion of pre-petition debt was classified as current

As discussed further in note 2, upon the Company's consummation of the Plan of Reorganization, all of XO Parent's pre-petition senior notes and pre-petition general unsecured claims were cancelled in exchange for (i) 4,750,000 shares of New Common Stock, (ii) warrants to purchase shares up to an additional 23,750,000 shares of New Common Stock (iii) rights to purchase shares of New Common Stock in the Rights Offering and (iv) a portion of the cash consideration received by XO Parent from the Investment Termination Payment Any holders of pre-petition subordinated notes of XO Parent had their securities cancelled, and received a cash payment from High River based upon the amount of the Investment Termination Payment that High River would have been entitled to receive as holder of the loans under the New Credit Agreement and the right to participate in the Rights Offering The pre-petition senior notes had interest rates ranging from 9 0% to 12 75% and the interest rate on the pre-petition convertible subordinated notes was 5 75%

The Pre-Petition Credit Facility bore interest at the Company's option, at an alternative base rate, as defined, or at the reserve-adjusted London Interbank Offered Rate ("LIBOR"), plus in each case, applicable margins As discussed further in note 2, upon the Company's consummation of the Plan of Reorganization, the $1 0 billion of loans under the Pre-Petition Credit Facility were converted into 90 25 million shares of New Common Stock and the $500 0 million of outstanding principal amount of loans under the New Credit Agreement The maturity date of the outstanding principal under the New Credit Agreement is July 15, 2009 and automatic and permanent quarterly reductions of the principal amount commence on October 15, 2007 The security for the New Credit Agreement consists of the all assets of XO Parent, including stock of its direct and indirect subsidiaries, and all assets of virtually all of those subsidiaries The New Credit Agreement limits additional indebtedness, liens, dividend payments and certain investments and transactions, and contains certain covenants with respect to minimum cash balance and EBITDA (earnings before interest, taxes, depreciation and amortization) requirements and maximum capital expenditures

The Company is not required to pay interest accrued on the principal amount under the New Credit Agreement until it meets certain financial ratios The Company can elect to begin paying interest in cash prior to the required date Loans under the New Credit Agreement bear interest, at the Company's option, at an alternate base rate, as defined, or LIBOR, plus in each case, applicable margins Once the Company begins to pay accrued interest in cash, the applicable margins are reduced Under certain circumstances, the New Credit Agreement permits the Company to obtain a senior secured facility of up to $200 0 million, subject to reduction in an amount equal to any proceeds received from the exercise of rights in the Rights Offering

During the second half of 2001, in a series of transactions, a subsidiary of the Company paid $201 9 million to repurchase $557 1 million of the outstanding principal of certain series of the pre-petition senior notes at a substantial discount to their respective face values As a result of these transactions, during the year ended December 31, 2001, the Company recognized an extraordinary gain of $345 0 million, net of unamortized financing costs

12. REDEEMABLE PREFERRED STOCK

As of December 31, 2002 and 2001, the carrying values of the Company's pre-petition preferred stock were $1 7 billion and $1 8 billion, respectively As discussed in note 2, as a result of the Company's emergence from bankruptcy and consummation of the Plan of Reorganization, the Company's pre-petition redeemable preferred stock has been cancelled and discharged and the holders of such securities will receive no distribution under the Plan of Reorganization

In conjunction with the implementation of the transactions that ultimately led to the reorganization of the Company's capital structure pursuant to the Plan of Reorganization, the Company ceased making all scheduled dividend payments effective December 31, 2001 and stopped accruing preferred stock dividends subsequent to the Petition Date In accordance with SOP 90-7, during the Chapter 11 proceedings, the Company was required to record its preferred stock at the amount allowed by the Bankruptcy Court Accordingly, during the second half of 2002, the Company recognized a gain equal to the remaining unamortized balance of a deferred modification fee and wrote off all issuance costs and discounts related to its preferred stock which resulted in a net gain of $78 7 million

During the second half of 2001, in a series of transactions, a subsidiary of the Company paid $88 4 million to repurchase $301 6 million in liquidation preference of its 14% pre-petition Series A senior exchangeable redeemable preferred stock and $171 0 million in liquidation preference of its pre-petition 13½% Series E senior redeemable exchangeable preferred stock at a substantial discount to their respective carrying amounts As a result of these transactions, the Company recognized a gain of $376 9 million, net of unamortized financing costs

13. STOCKHOLDERS' EQUITY

In December 2001, the Company voluntarily delisted its pre-petition Class A common stock from the Nasdaq National Market and began trading on the Nasdaq Over-the-Counter Bulletin Board ("OTCBB") on December 17, 2001 under the symbol "XOXO" The Company's pre-petition Class A common stock stopped trading on the OTCBB as of the Effective Date and the New Common Stock began trading on the OTCBB under the symbol "XOCM" shortly thereafter As discussed in note 2, pursuant to the Plan of Reorganization, all interests in the Company's pre-petition Class A and Class B common stock were terminated as of the Effective Date

On June 7, 2001, an investment fund affiliated with Forstmann Little invested $250 0 million of cash in the Company to provide additional funding for general corporate purposes In exchange for the investment, the Company issued 50 0 million shares of its pre-petition Class A common stock to the Forstmann Little fund and amended the terms of outstanding pre-petition convertible preferred stock held by various funds affiliated with Forstmann Little to reduce the share conversion price from $31 625 to $17 00 per share The value of the pre-petition Class A common stock issued at the date the investment closed was $157 5 million The remaining $92 5 million, attributed to the pre-petition convertible preferred stock amendment, was recorded as a credit to the preferred stock balance and was being amortized against the accretion of the preferred stock redemption obligation As discussed in note 12, during the second half of 2002, the Company recognized a gain equal to the remaining unamortized balance of this deferred modification fee

In June 2000, the Company effected two-for-one stock splits of the issued and outstanding shares of pre-petition Class A and Class B common stock, in the form of stock dividends The accompanying consolidated financial statements and the related notes herein have been adjusted retroactively to reflect the two-for-one stock splits

14. INCOME TAXES

Components of deferred tax assets and liabilities were as follows (dollars in thousands)

	December 31, 2002	December 31, 2001
Deferred tax assets		
Provisions not currently deductible	$ 123,280	$ 41,954
Property, equipment and other long-term assets (net)	367,208	348,582
Net operating loss and capital loss carryforwards	1,863,336	1,313,477
Total deferred tax assets	2,353,824	1,704,013
Valuation allowance	(2,028,331)	(1,390,017)
Net deferred tax assets	325,493	313,996
Deferred tax liabilities		
Property, equipment and other long-term assets (net)	(101,402)	(72,108)
Other identifiable intangibles	(222,537)	(238,465)
Other	(1,554)	(3,423)
Total deferred tax liabilities	(325,493)	(313,996)
Net deferred taxes	$ —	$ —

The net change in valuation allowance for the year ended December 31, 2002 was an increase of $638 3 million The net change in the valuation allowance for years ended December 31, 2001 and 2000 was an increase of $591 2 million and $521 2 million, respectively

As of December 31, 2002, the Company has capital loss carryforwards of approximately $0 5 billion and net operating loss carryforwards of approximately $4 0 billion As discussed in notes 2 and 3, upon consummation of the Plan of Reorganization during the first quarter of 2003, the Company will recognize a substantial amount of cancellation of indebtedness income Accordingly, a substantial portion of the Company's $4 5 billion of capital and net operating loss carryforwards are expected to be eliminated Other tax attributes, including property bases, could also be reduced Any surviving capital or net operating loss carryforwards will be subject to limitations imposed under the ownership change rules in the U S Internal Revenue Code

The Company will join with the affiliated group of corporations controlled by Mr Icahn in filing a consolidated federal income tax return As such, the Company entered into a Tax Allocation Agreement with Starfire Holding Corporation ("Starfire"), the Parent entity of the affiliated group of corporations controlled by Mr Icahn Generally, the Tax Allocation Agreement provides that Starfire will pay all consolidated federal income taxes on behalf of the consolidated group that includes XO, and XO will make payments to Starfire in an amount equal to the tax liability, if any, that it would have if it were to file as a consolidated group separate and apart from Starfire

A reconciliation of the Company's effective income tax rate and the U S federal and state tax rate is as follows

	2002	2001
Statutory U S federal rate	35 0%	35 0%
State income taxes, net of federal benefit	6 0%	6 0%
Valuation allowance for deferred tax assets	(18 3%)	(29 4%)
Other identifiable intangibles	(22 7%)	(11 6%)
Effective income tax rate	— %	— %

15. COMPREHENSIVE LOSS

Comprehensive loss includes the Company's net loss applicable to common shares, as well as net unrealized gains and losses on available-for-sale investments and foreign currency translation adjustments from the Company's former European operations, which were sold in February 2002 The following table reflects the Company's calculation of comprehensive loss for the years ended December 31, 2002, 2001 and 2000 (dollars in thousands)

	Year Ended December 31,		
	2002	2001	2000
Net loss applicable to common shares	$ (3,350,362)	$ (1,838,917)	$ (1,247,655)
Other comprehensive (gains) loss			
Net unrealized holding (gains) losses and foreign currency translation adjustments	—	22,556	38,870
Less Net realized (gains) losses and foreign currency translation adjustments transferred to current period earnings	(7,894)	4,891	(206,545)
Comprehensive loss	$ (3,358,256)	$ (1,811,470)	$ (1,415,330)

16. STOCK COMPENSATION ARRANGEMENTS

The Company had an Employee Stock Purchase Plan, (the "Purchase Plan"), under which 12 0 million shares of Class A common stock were authorized for issuance The Purchase Plan was suspended in 2001 in connection with the commencement of XO Parent's balance sheet reorganization, and then was subsequently cancelled As discussed in note 2, pursuant to the Plan of Reorganization, all interests in the Company's pre-petition Class A common stock were terminated as of the Effective Date Prior to the suspension of the Purchase Plan, eligible employees could purchase the Company's pre-petition Class A common shares at 85% of the lower of the average market value of the Class A common stock on the first and the last trading day of each calendar quarter Employees who owned 5% or more of the voting rights of the Company's outstanding common shares could not participate in the Purchase Plan During the years ended December 31, 2001 and 2000, employees purchased 6 3 million and 0 4 million shares of pre-petition Class A common stock, respectively, under the Purchase Plan

Prior to the Effective Date, the Company also maintained the XO Communications, Inc Stock Option Plan (the "Stock Option Plan") and certain other equity compensation plans that had been assumed in connection with the acquisition of Concentric Network (collectively, the "Old Stock Option Plans") to provide a performance incentive for certain officers, employees and individuals or companies who provide services to the Company The Old Stock Option Plans provided for the granting of qualified and non-qualified stock options The options became exercisable over vesting periods of up to four years and expired no later than 10 years after the date of grant

The Company had authorized 113 0 million shares of pre-petition Class A common stock for issuance under the Old Stock Option Plans In May 2001, the Company offered its employees the opportunity to exchange certain options outstanding under the Old Stock Option Plans for new options equal to 85% of the number of shares tendered The Company granted the new options on January 17, 2002, the first business day that was six months and one day following the closing of this exchange offer The exercise price of the new options was the last reported sale price of the pre-petition Class A common stock on the date of that grant, which was $0 14 per share The new options were 30% vested on the date of grant and the remaining 70% vest monthly in equal installments over the following 36-month period until fully vested As of December 31, 2002, 44 0 million shares were available for issuance under the Old Stock Option Plans However, as discussed in note 2 under the Plan of Reorganization, all interests in the Company's pre-petition Class A common stock including any options or awards granted under the Old Stock Option Plans, were terminated and cancelled as of the Effective Date, and holders of such options under such plans were entitled to no distribution pursuant to the Plan of Reorganization

The Company recorded approximately $28 9 million, $37 2 million, and $48 3 million of stock-based compensation expense related to the Old Stock Option Plan for the years ended December 31, 2002, 2001, and 2000, respectively

The following two tables summarize information regarding options under the Company's Old Stock Option Plan for the last three years

	Number of Shares	Weighted Average Exercise Price
Outstanding at December 31, 1999	55,203,534	$ 9 86
Assumed in acquisition	13,086,985	$ 20 51
Granted	36,850,732	$ 35 17
Canceled	(12,590,334)	$ 19 52
Exercised	(11,310,416)	$ 6 63
Outstanding at December 31, 2000	81,240,501	$ 22 77
Granted	5,909,809	$ 7 72
Canceled	(49,163,452)	$ 28 32
Exercised	(3,677,562)	$ 5 36
Outstanding at December 31, 2001	34,309,296	$ 13 91
Granted	24,978,119	$ 0 14
Canceled	(15,053,582)	$ 9 97
Exercised	(35,860)	$ 0 01
Outstanding at December 31, 2002	44,197,973	$ 7 37
Exercisable, at December 31, 2000	16,369,892	$ 11 30
Exercisable, at December 31, 2001	18,902,125	$ 12 38
Exercisable, at December 31, 2002	30,350,882	$ 8 00

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Options Outstanding at December 31, 2002	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Options Exercisable at December 31, 2002	Weighted Average Exercise Price
$0 01 - $0 16	22,929,528	8 6	$ 0 12	13,097,978	$ 0 11
$0 25 - $6 25	5,892,586	6 1	$ 4 26	4,818,112	$ 4 68
$6 28 - $14 06	8,416,102	6 5	$ 9 61	7,521,309	$ 9 39
$14 25 - $66 00	6,959,757	6 9	$ 31 16	4,913,483	$ 30 16
	44,197,973	7 6	$ 7 37	30,350,882	$ 8 00

The Company uses the Black-Scholes option-pricing model to determine the pro forma effect of using the intrinsic value method rather than the fair value method of accounting for employee stock options The model uses certain information, such as the interest rate on a risk-free security maturing generally at the same time as the option being valued, and requires certain assumptions, such as the expected amount of time an option will be outstanding until it is exercised or it expires, to calculate the weighted average fair value per share of stock options granted This information and the assumptions used for 2002, 2001, and 2000 are summarized below

	2002	2001	2000
Expected volatility	125 0%	125 0%	77 2%

Risk free interest rate	4 0%	4 3%	6 2%
Dividend yield	0 0%	0 0%	0 0%
Expected life (range in years)	4 0	4 0	4 0
Weighted average fair value per share at grant date	$0 11	$5 10	$19 14

In connection with the confirmation of the Company's Plan of Reorganization, the Bankruptcy Court approved the adoption of the XO Communications, Inc 2002 Stock Incentive Plan (the "2002 Stock Incentive Plan"), as of the Effective Date Under the 2002 Stock Incentive Plan, the Company is authorized to issue, in the aggregate, stock awards of up to 17 6 million of shares of New Common Stock, in the form of options to purchase stock or restricted stock Non-qualified options to purchase 11 5 million shares of the New Common Stock have been granted and are outstanding as of March 1, 2003, each at a purchase price of $5 00 per share Of these options, 25% are vested and the remainder vest over three years

The 2002 Stock Incentive Plan is administered by the Compensation Committee of the Company's Board of Directors, which has the discretionary authority to determine all matters relating to awards of stock options and restricted stock, including the selection of eligible participants, the number of shares of common stock to be subject to each option or restricted stock award, the exercise price of each option, vesting, and all other terms and conditions of awards

Unless the Compensation Committee designates otherwise, all options expire on the earlier of (i) ten years after the date of grant, (ii) twelve months after termination of employment with XO due to death or complete and permanent disability, (iii) immediately upon termination of employment by XO for cause, or (iv) three months after termination of employment by the employee or by XO for other than cause

17. SUPPLEMENTAL DISCLOSURE OF CASH FLOW DATA

Supplemental disclosure of the Company's cash flow information is as follows (dollars in thousands)

	Year Ended December 31,		
	2002	**2001**	**2000**
Non-cash financing and investing activities were as follows			
Class A common stock, warrants and options issued in acquisitions and under lease arrangements	$ —	$ 29,055	$ 3,002,309
Redeemable preferred stock dividends, paid in shares of redeemable preferred stock	—	86,237	76,671
Accrued redeemable preferred stock dividends, payable in shares of redeemable preferred stock	—	6,524	17,090
Assumption of preferred stock and liabilities in acquisitions	—	8,816	614,027
Conversion of 6½% redeemable cumulative preferred stock to Class A common stock	35	17,700	93,860
Other obligations assumed	—	—	11,119
Cash paid for interest	$ 11,681	$ 313,178	$ 331,892

As discussed in note 2, the Company ceased paying dividends and interest on its redeemable preferred stock and its senior unsecured notes during 2001 and its subordinated unsecured notes in February 2002

Employee Savings and Retirement Plan

At December 31, 2002, the Company had a defined contribution plan, generally covering all full time employees in the United States The Company provides a company match to all eligible employees based on certain plan provisions and the discretion of the Board of Directors Beginning November 30, 2001, the Company's pre-petition Class A common stock was no longer available as an investment option due to the Company's pending reorganization Effective April 1, 2002, the Company changed its employer matching contribution from a 100% matching contribution up to 5% of the participant's compensation to a 50% matching contribution up to 5% of the participant's compensation Company contributions were $ 7 0 million, $12 5 million and $8 3 million during 2002, 2001 and 2000, respectively

18. OPERATING SEGMENTS

Reportable Segments

The Company operates its business as one communications segment The Company's communications segment includes all of its products and services including data, voice, integrated voice and data, and other services These services have similar network operations and technology requirements and are sold through similar sales channels to a similar targeted customer base Therefore, the Company manages these services as a single segment that is divided into profit centers that are focused on geographic areas, or markets, within the United States, or that are focused on customers with a presence across geographical markets

Products and Services

The Company classifies its products and services revenues offered by its communications services segment into voice services, data services, integrated voice and data services, and other services (dollars in thousands)

	Year Ended December 31,		
	2002	2001	2000
Voice services	$ 658,453	$ 606,848	$ 386,796
Data services	472,247	596,664	331,892
Integrated voice and data services	128,048	52,018	2,693
Other services	1,105	3,037	2,445
Total revenue	$ 1,259,853	$ 1,258,567	$ 723,826

19. SELECTED QUARTERLY DATA (Unaudited)

Quarterly financial information is summarized in the table below (dollars in thousands, except for share data)

	Quarter ended 2002			
	March 31,	June 30,	September 30,	December 31,
Revenue	$ 333,405	$ 325,480	$ 301,526	$ 299,442
Cost of service	140,367	134,346	126,215	121,996
Loss from operations (a) (b)	(182,663)	(176,771)	(673,001)	(176,463)
Net loss before extraordinary item and cumulative effect of accounting change	(299,028)	(346,133)	(695,209)	(169,822)
Net loss (c)	(2,175,654)	(346,133)	(695,209)	(169,822)
Net loss applicable to common shares (d)	(2,198,480)	(286,851)	(695,209)	(169,822)
Net loss per common share (basic and diluted) (e)	(4 97)	(0 65)	(1 57)	(0 39)

	Quarter ended 2001			
	March 31,	June 30,	September 30,	December 31,
Revenue	$ 277,307	$ 306,779	$ 331,478	$ 343,003
Cost of service	114,894	122,942	138,100	151,762
Loss from operations (a)	(358 248)	(362,418)	(547,285)	(681,940)
Net loss before extraordinary item	(443,511)	(461,116)	(734,655)	(791,853)
Net loss (c)	(443,511)	(461,116)	(398,917)	(782,581)
Net loss applicable to common shares (d)	(482,552)	(500,722)	(50,752)	(804,891)
Net loss per common share (basic and diluted) (e)	(1 31)	(1 32)	(0 12)	(1 84)

a In the third quarter of 2002, loss from operations includes a non-cash asset write down totaling $477 3 million resulting from an agreement with Level 3 to amend various agreements relating to the Company's Level 3 inter-city fiber network facilities. In the second quarter of 2001, loss from operations includes restructuring charges totaling $509 2 million associated with plans to restructure certain aspects of the Company's business operations

b Loss from operations in the quarters ended March 31, June 30, and September 30, 2002, respectively, reflects the reclassification of reorganization expense, net to below loss from operations

c In the first quarter of 2002, net loss includes a $1,876 6 million impairment charge to write-off all of XO's goodwill as a cumulative effect of accounting change, pursuant to SFAS No 142 In the third quarter of 2001, net loss includes an extraordinary gain of $345 0 million resulting from the repurchase of certain of XO's senior notes and a write-down of $87 0 million for an other than temporary decline in the value of certain investments

d In the second quarter of 2002 net loss applicable to common shares includes a net gain of $78 7 million as XO's preferred stock was deemed subject to compromise under SOP 90-7 as of the Petition Date, requiring the Company to recognize the remaining $81 5 million unamortized balance of its deferred modification fee and write-off certain issuance costs and discounts.

e The net loss per share data has been calculated based on the shares outstanding of the Company's pre-petition class A and class B common stock prior to the consummation of its Plan of Reorganization. On the Effective Date of the Company's Plan of Reorganization, all interests in XO's pre-petition class A and class B common stock were terminated and all outstanding shares were cancelled. See note 2 for further discussion The net loss per share data has been adjusted for the stock splits effected in 2000 and in prior periods

20. RELATED PARTY TRANSACTIONS

In February 2003, Dixon Properties, LLC ("Dixon"), which is controlled by Mr Icahn, acquired ownership of the building in which XO headquarters is located in a transaction that was approved by the Bankruptcy Court XO currently leases approximately 170,000 square feet of space in that building In connection with the purchase of the building by Dixon, it assumed the existing lease agreement Pursuant to the assumed lease agreement, XO is obligated to pay $20 4 million in the aggregate to Dixon through the expiration of the initial term of the lease, which is November 30, 2007

XO Parent has entered into a Tax Allocation Agreement, dated January 16, 2003, between XO Parent and Starfire, a company controlled by Mr Icahn, which in turn indirectly controls Cardiff, in connection with the fact that it is contemplated that these entities will be filing consolidated federal income tax returns, and possibly combined returns for state tax purposes The Tax Allocation Agreement, which was approved by the Bankruptcy Court in connection with XO Parent's Chapter 11 proceedings, establishes the methodology for the calculation and payment of income taxes in connection with the consolidation of the Company with Starfire for income tax purposes Generally, the Tax Allocation Agreement provides that Starfire will pay all consolidated federal income taxes on behalf of the consolidated group that includes the Company, and the Company will make payments to Starfire in an amount equal to the tax liability, if any, that it would have if it were to file as a consolidated group separate and apart from Starfire

Arnos, which is owned and controlled by Mr Icahn, holds approximately 85% of the $500 million in loans outstanding under the New Credit Agreement Under the New Credit Agreement, no cash interest payments are required to be made by the Company until it achieves specified financial targets

In July 2001, the Company executed a multi-year agreement with Nextel Communications, Inc ("Nextel") pursuant to which XO will provide Nextel telecommunications services Individuals who served as members of the Company's board of directors prior to the Effective Date of the Company's Plan of Reorganization also serve on the board of directors of Nextel One of these members, Craig O McCaw, along with his affiliates, held a controlling voting interest in the Company prior to the Effective Date of the Plan of Reorganization and holds certain management rights related to his investment in Nextel Prior to entering into the agreement with Nextel, the Company participated in a competitive proposal process initiated by Nextel, which included numerous national telecommunications providers Therefore, in management's opinion, the agreement with Nextel was consummated in the normal course of operations with prices and terms equivalent to those available to, and transacted with, unrelated parties

Prior to the Effective Date of the Company's Plan of Reorganization, certain investment funds affiliated with Forstmann Little & Co had a significant equity interest in the Company and had designated certain individuals to serve as members of the Company's board of directors Such investment funds and other entities affiliated with Forstmann Little & Co also hold a significant equity interest in McLeodUSA ("McLeod") McLeod provides interconnection and facilities based telecommunications services to the Company, and the Company provides, on a limited basis, telecommunications service to McLeod In addition, during 2001, XO acquired certain unlit metro network capacity from McLeod to support infrastructure requirements in a specific XO market

The following table summarizes the Company's transactions with Nextel and McLeod (dollars in thousands)

	Revenue recognized from services provided for the year ended December 31,		Payments made for services received for the year ended December 31,	
	2002	2001	2002	2001

McLeod	$ 373	$ 7,112	$ 1,953	$ 8,410
Nextel	$ 66,852	$ 27,599	$ 2,745	$ 6,206

The following amounts are outstanding as a result of the Company's transactions (dollars in thousands)

	Accounts receivable as of December 31,		Accounts payable as of December 31,	
	2002	2001	2002	2001
McLeod	$ 16	$ 57	$ 20	$ -
Nextel	$ 11,219	$ 9,732	$ -	$ 10

21. COMMITMENTS AND CONTINGENCIES

Operating Commitments

The Company is leasing premises under various noncancelable operating leases for administrative space, building access, and other leases, which, in addition to rental payments, require payments for insurance, maintenance, property taxes and other executory costs related to the leases The lease agreements have various expiration dates and renewal options through 2021 The Company also has various noncancelable long-term contractual obligations associated with maintenance and service agreements

Future minimum lease commitments required under noncancelable operating leases and contractual obligations are as follows (dollars in thousands)

Year Ending December 31,	Operating lease obligations	Other long-term contractual obligations
2003	$ 62,733	$ 74,126
2004	59,045	57,612
2005	55,600	17,574
2006	51,458	14,577
2007	47,334	11,780
Thereafter	232,550	107,277
Total minimum commitments	$ 508,720	$ 282,946

Rent expense for cancelable and noncancelable leases totaled approximately $76 4 million, $100 1 million, and $54 6 million for the years ended December 31, 2002, 2001, and 2000, respectively

Capital Leases

Network assets under capital leases totaled approximately $16 3 million and $27 2 million as of December 31, 2002 and 2001, respectively, and are included in telecommunications networks in property and equipment Depreciation on leased assets of $2 0 million for the year ended December 31, 2002 is included in depreciation expense Future minimum lease payments under capital lease obligations as of December 31, 2002 are as follows (dollars in thousands)

Year Ending December 31,	
2003	$ 10,031
2004	2,809
2005	2,668
2006	2,416
2007	1,733
Thereafter	277
Total minimum capital lease payments	19,934
Less imputed interest	4,123
Less current portion of capital lease obligations	8,629

Long-term portion of capital lease obligation	$ 7,182

As of December 31, 2002 both the current portion and long-term portions of the capital lease obligation are classified as subject to compromise, in accordance with SOP 90-7

Legal Proceedings

The Company is not currently a party to any legal proceedings, other than regulatory and other proceedings that are in the normal course of business

Prepaid Calling Card Tax Matter

On July 26, 2002, the Company was advised by the staff of the Securities and Exchange Commission that it was conducting an informal inquiry primarily relating to obligations with respect to, and XO's accrual of liabilities for, specified federal excise and state sales tax and similar tax obligations arising in connection with prepaid calling card services and relating to certain other matters Sales from prepaid calling card services that are potentially subject to these taxes accounted for approximately $56 million of total revenues for 1999, when the Company began providing these services, through June 30, 2002 The Company believes that its accounting for these potential obligations is appropriate and that its accruals of liabilities relating to these obligations are adequate

Unfunded Affiliate Pension Obligation

As discussed in note 2, affiliates of Mr Icahn hold over 80% of the outstanding New Common Stock of XO Parent Applicable pension and tax laws make each member of a plan sponsor's "controlled group" (generally defined as entities in which there is at least an 80% common ownership interest) jointly and severally liable for certain pension plan obligations of the plan sponsor These pension obligations include ongoing contributions to fund the plan, as well as liability for any unfunded liabilities that may exist at the time the plan is terminated In addition, the failure to pay these pension obligations when due may result in the creation of liens in favor of the pension plan or the Pension Benefit Guaranty Corporation, (the "PBGC") against the assets of each member of the plan sponsor's controlled group

As a result of the more than 80% ownership interest in XO Parent by Mr Icahn's affiliates, XO Parent and its subsidiaries will be subject to the pension liabilities of any entities in which Mr Icahn has a direct or indirect ownership interest of at least 80%, which includes ACF Industries, Inc ("ACF"), which is the sponsor of certain pension plans As most recently determined by the ACF plans' actuaries, pension plans maintained by ACF are underfunded in the aggregate by approximately $14 million on an ongoing actuarial basis and by approximately $102 million if those plans were terminated As a member of the same controlled group, XO Parent and each of its subsidiaries would be liable for any failure of ACF to make ongoing pension contributions or to pay the unfunded liabilities upon a termination of the ACF pension plans

The current underfunded status of the ACF pension plans requires ACF to notify the PBGC if XO Parent or its subsidiaries cease to be a member of the ACF controlled group In addition, so long as the Company remains a member of the ACF controlled group, certain other "reportable events," including certain extraordinary dividends and stock redemptions, must be reported to the PBGC

22. SUBSEQUENT EVENT

Effectiveness of Bankruptcy Plan

The Plan of Reorganization that was confirmed by order of the Bankruptcy Court on November 15, 2002 became effective January 16, 2003, and is discussed in more detail in note 2

XO Communications, Inc.
Schedule II - Consolidated Valuation and Qualifying Accounts
For The Years Ended December 31, 2002, 2001 and 2000

(in thousands)	Beginning Balance	Additions charged to expense	Reductions	Ending Balance
Allowance for doubtful accounts				
2000	$ 7,215	$ 21,999	$ (8,215)	$ 20,999
2001	$ 20,999	$ 45,757	$ (34,264)	$ 32,492
2002	$ 32,492	$ 53,631	$ (49,093)	$ 37,030
Restructuring accrual				
2000	$ 30,935	$ —	$ (30,935)	$ —
2001 (a)	$ —	$ 509,202	$ (383,429)	$ 125,773
2002 (b)	$ 125,773	$ 480,168	$ (526,951)	$ 78,990

(a) Only $16 6 million of the reduction in the 2001 restructuring accrual was for cash payments The balance was associated with the write down for the excess of carrying value of assets to be sold or abandoned and was applied to those assets

(b) Only $49 7 million of the reduction in 2002 restructuring accrual was for cash payments The balance was associated with the non-cash asset write down resulting from an agreement with Level 3 to amend various agreements relating to XO's Level 3 inter-city fiber network facilities